Association of Financial Advisers

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Competition in Australia’s Financial System Inquiry
Productivity Commission
GPO Box 1428
Canberra City ACT 2601

Dear Productivity Commission,

AFA Submission – Consultation: Competition in the Australian Financial System

The Association of Financial Advisers Limited (**AFA**) has served the financial advice industry for over 70 years. Our objective is to achieve *Great Advice for More Australians* and we do this through:

- advocating for appropriate policy settings for financial advice
- enforcing a Code of Ethical Conduct
- investing in consumer-based research
- developing professional development pathways for financial advisers
- connecting key stakeholders within the financial advice community
- educating consumers around the importance of financial advice

The Board of the AFA is elected by the Membership and all Directors are practicing financial advisers. This ensures that the policy positions taken by the AFA are framed with practical, workable outcomes in mind, but are also aligned to achieving our vision of having the quality of relationships shared between advisers and their clients understood and valued throughout society. This will play a vital role in helping Australians reach their potential through building, managing and protecting wealth.

Introduction

The AFA welcomes the opportunity to make a submission in response to the Productivity Commissions Draft Report on Competition in the Australian Financial system.

We note the Productivity Commissions concern about the level of competition in the Australian financial system. We support some of the comments about the impact of the Future of Financial Advice reforms. Whilst one of the objectives of that reform package was to improve access to advice, this has not eventuated. One of the core factors in this is that the cost of providing financial advice has increased materially over the last few years as a range of different reforms have been implemented and as standards have been increased. It has been the cumulative effect of these changes that has significantly increased costs and as a result is now challenging the financial advice professional and individual advice practices to economically service the average Mum and Dad market. It is critically important that young people and the less wealth can continue to access financial advice.

We note the discussion in the report on the introduction of "robo advice" and the expectation that this will emerge as a new more efficient form of financial advice. We make the point that robo advice is limited to simple advice with respect to a specific matter, such as re-balancing a superannuation fund investment allocation. It typically does not address complex matters. It is equally important to recognise that some of the key benefits of financial advice, which include increased financial knowledge, a sense of financial direction and security, and changed financial behaviours, will only come with the benefit of an ongoing adviser relationship that in most cases is likely to be delivered face-to-face. Robo advice will continue to develop and will become an important part of the advice sector, but predominantly in simple transaction based areas. Robo advice will increasingly become a tool to initially engage with new clients, although these relationships are expected to evolve to be more personal over time.

We note the reference in the Draft Report to the comment on the MoneySmart website that simple advice could be as cheap as $200-$700. When the full obligations of preparing financial advice are taken into consideration, this is inevitably significantly underestimating the real cost of financial advice. ASIC recently released their example Risk Insurance Statement of Advice (SoA), which is a document that includes over 20 pages of carefully tailored material. Personal advice provided to a new retail client with respect to a superannuation, investment or insurance product, must in almost all circumstances be provided by the means of an SoA. Before providing the advice, the financial adviser must undertake a fact finding exercise to adequately understand the client's needs, objectives and personal circumstances. They also need to undertake a number of other steps including researching product options that are appropriate for the client. There is a significant amount of work involved in the provision of financial advice.

As the Productivity Commission has pointed out, there is a lack of awareness by consumers of the cost of providing financial advice and along with other assumptions leads to a lack of willingness to pay for the true cost of financial advice. There is much work that needs to be done to better ensure that consumers are aware of the cost of financial advice and are also willing to pay for the true cost of high quality financial advice that is in their best interests.

A number of the issues identified in the Draft Report and items discussed above highlight the issue in Australia with financial literacy. The AFA strongly supports the objective that financial advice clients engage in the financial advice process and provide informed consent with respect to their financial decisions. We do not believe that it is acceptable that they simple agree to the decision that their adviser makes. It is important that they genuinely understand what the adviser has recommended, and they consciously endorse the decision. Achieving improved levels of financial literacy will ensure that Australians are better prepared for seeking and receiving financial advice and will get the most benefits from obtaining that advice. For this reason, we believe that more needs to be done to improve the level of financial literacy.

We have primarily focused our feedback in the sections below, on the matters that more directly relate to the financial advice sector.

Response to Recommendations and Requests Raised in the Draft Paper

Information Request 12.1 – Potential to Increase the Scope of Financial Advice to Include some Credit Products

The AFA supports this proposal. Financial advisers can choose to be licensed under both the AFSL and Credit regimes. This outcome however adds to cost and complexity and over time many have stepped back from the Credit licensing regime. This limits the advice that they can provide to their clients, even when it might be high level or strategic advice where they would not have intended to play a role in implementing the decisions for clients. This is particularly the case where advisers are providing advice on cashflow management or budgeting. Such advice may include matters such as paying down loans that have the highest rate of interest. When specific products are mentioned, this becomes advice and disclosure obligations apply.

The primary products related to advice on credit include home loans, personal loans and credit cards. It is also very common for financial advisers to provide advice with respect to mortgage offset accounts, which are classified as financial products.

In terms of the duty that would apply, in our view it would need to be the best interests duty which applies to personal advice that is provided with respect to financial products.

From our perspective the best solution is to modify the Corporations Act in some way in order to enable peripheral advice on these credit products to be provided under an AFSL.

We do not believe that there would be significant regulatory cost or impact to the industry. From our perspective this is largely a reform to enable financial advisers to give a more comprehensive service to their clients, but in a way where there is only upside for consumers. In many cases, rather than getting this advice from another source, consumers are going without this advice.

Draft Recommendation 12.1 – Rename General Advice to Improve Consumer Understanding

The issue of general advice is an area where we often receive feedback from our members. The obligations when providing personal advice are substantial. The obligations when providing general advice are significantly less. The core distinction is whether the advice relied upon knowledge of the customer's personal circumstances. The difference in terms of the discussion with the customer between personal advice and general advice can sometimes be very minimal. Our members regularly provide feedback on business models that run very close to this boundary. In providing advice on life insurance, it is critical that an adviser understands the assets and liabilities of the client, their income and expenses and the details about their dependents. Direct insurance, provided via the means of general advice necessarily needs to be based upon the customer deciding what is right for them. Most customers do not have sufficient understanding to determine this, which means that they are either inappropriately assisted in that decision or otherwise the wrong choice is made. As part of the sales process, the representative is likely to make reference to general advice, when providing the general advice warning.

We support the proposal to rename general advice and note that this has been an issue that has been subject to debate for some time. This same issue was addressed in recommendation 40 of the Financial System Inquiry back in December 2014.

Whilst we agree that there are issues with the term general advice, however we also note that this term is not one that has particular meaning to clients. We believe that the issues with general advice are deeper and relate back to the obvious risk that sometimes general advice is actually personal advice and this leaves customers in a significantly disadvantaged position. Nonetheless, we support measures that will contribute to minimising the risk that consumers think they are getting advice, when they are not.

Information Request 12.2 – Renaming General Advice and Merits of Further Changes

From a financial advice perspective, this change would not have a significant impact upon costs. Financial advisers do have some documents that might refer to general advice, however these are already changed on a regular basis and could be updated relatively easily if there was a transition period of 12 months. They are also increasingly provided to customers in an electronic format rather than in hard copy.

There are no unintended consequences that we are aware of with respect to financial advisers who provide personal advice.

Whilst supporting the renaming of general advice, we believe that there is merit in considering a broader review of the general advice model to ensure that the way that it is used best ensures that the consumer gets a good outcome. This could include placing more obligations on the people who use this model to provide advice.

We do not support removing licensing and regulatory obligations for people providing general advice. Where the general advice model can be used to sell financial products then there should be licensing and regulatory obligations in order to achieve the required levels of protection for consumers.

Draft Finding 7.1 – Consolidation in Asset Management and Financial Advice

We note this finding, however suggest that consolidation in financial advice now appears to have turned the corner and more advisers are leaving large licensees rather than joining. This point is made in the following Adviser Ratings article (http://www.adviserratings.com.au/news/licensee-movement-analysis/)

There appears to be a number of factors in play here including an increased desire by some financial advisers for greater independence and autonomy.

We would also make the comment that there is currently a substantial range of product choice for both financial advisers and their clients to choose from. We do not believe that this has worked to the disadvantage of consumers.

Financial advice has gone through a period of substantial change over the last 10 years, which is having a broad range of impacts upon the sector. Key amongst these is the impact on the cost of running a financial advice practice and providing financial advice. Negative media coverage has also impacted consumer choice in seeking advice. Financial advisers now face substantial increases in their education standards, which is likely to lead to a reduction in new entrants to the profession and a significant increase in exits. This will have broad economic impacts, including a reduction in access to financial advice and an increase in the cost of financial advice.

Concluding Remarks

The AFA welcomes the opportunity to contribute to this review. If you have any questions, then please contact us

Yours faithfully

Philip Kewin
Chief Executive Officer
Association of Financial Advisers Ltd